



DEPARTMENT OF JUSTICE

Antitrust Division

A. Douglas Melamed

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January 10, 2001

Steven Napper, Esq.
Steven Napper, Ltd.
201 S. Chester
Little Rock, Arkansas 72201

Dear Mr. Napper:

This is in response to your request on behalf of seventeen rural electric distribution cooperatives ("the Distribution Cooperatives") in Arkansas and their joint venture, Arkansas Electric Cooperative Corporation ("AECC") for the issuance of a business review letter pursuant to the Department of Justice's Business Review Procedure, 28 C.F.R. § 50.6. You have requested a statement of the Department of Justice's antitrust enforcement intentions with respect to the proposal of the Distribution Cooperatives to engage in the retail sale of electric power on a state-wide basis through a joint selling agent.

The Distribution Cooperatives are seventeen nonprofit cooperative corporations formed pursuant to the Electric Cooperative Corporation Act of Arkansas to provide electric service predominantly to rural consumers. Each of the Distribution Cooperatives is owned by the individual member/consumers that it serves and is legally obligated to distribute annually all of its income to its member/customers.

Sixteen of the Distribution Cooperatives currently own and operate a joint venture called Arkansas Electric Cooperative Corporation which was formed as a cooperative in 1949 for the purpose of providing a stable source of low-cost electricity for those Distribution Cooperatives.¹ These Distribution

¹ The seventeenth distribution cooperative is not presently a member of and does not purchase electricity from

Cooperatives, through AECC, currently own all of, or interests in, ten electric power generation plants. AECC provides electric power, on a nonprofit basis, for these Distribution Cooperatives on an all-requirements basis through its electric generation facilities and through wholesale power purchases. The Distribution Cooperatives, in turn, sell electricity to their respective member/customers on a nonprofit basis.

In 1999, Arkansas enacted the Electric Consumer Choice Act of 1999, (the "Act") mandating competition in the retail sale of electricity beginning as early as January 1, 2002. The Act will significantly change the way retail electricity is purchased and sold within the State of Arkansas. Currently, retail consumers may purchase electric energy only from the regulated electric utility serving the territory in which the consumer is located. Under the Act, a consumer will be allowed to purchase electric energy from anyone in the competitive marketplace, and the consumer's incumbent utility will have to deliver that electricity to the consumer's door under regulated distribution charges.

You indicate that the primary focus of the new legislation is the separation of the retail marketing activities, which will be completely competitive, from the electric utility's regulated transmission and distribution activities. In order to ensure that the utility's marketing operations do not benefit improperly from its relationship with the utility, the Act provides that the utility must conform to certain specified affiliate rules or codes of conduct. These rules generally provide that employees of an affiliate engaged in the transmission and distribution system operations must function independently of employees engaged in the marketing or sale of electricity at retail.

The Act also creates an obligation for each incumbent utility to offer a standard service package to any consumer that has not elected an alternative energy service provider or to any consumer that has not been able to secure an alternative energy service provider. Such consumers are commonly referred to as "default customers". Under the provisions of the Act, each of the Distribution Cooperatives may serve its default customers directly or assign them to an affiliate. The rates for the

AECC, but it is expected to become a member in the future.

standard service package will be a market rate unless the incumbent utility chooses to offer a regulated rate approved by the Arkansas Public Service Commission ("PSC").

The Distribution Cooperatives propose using their existing joint venture, AECC, to create an energy service provider (the "ESP") to enter retail electric competition in Arkansas. Under the ESP's operating agreement, the Distribution Cooperatives will agree to conduct all of their retail marketing activities outside of their traditional territories through the ESP. If a Distribution Cooperative decides to withdraw from the ESP, the departing Distribution Cooperative may compete with the ESP for any and all consumers. Each Distribution Cooperative will individually decide whether to serve its default customers directly or to assign them to the ESP.

It is anticipated that a large majority of the Distribution Cooperatives will elect to retain their default customers for themselves rather than assigning them to the joint venture and will further elect to provide a regulated rate to the default customers as approved by the PSC. The ESP will be permitted to compete for these customers. Although the ESP is likely initially to focus its energies on gaining retail customers outside of the territories of its members, it will eventually compete with the Distribution Cooperatives to serve the default customers.

The information that you have provided indicates that each of the Distribution Cooperatives has a relatively small amount of the electric power generating capacity in the State of Arkansas. Indeed, the combined generating power capacity of all of the Distribution Cooperatives is approximately six percent of the total generating capacity in the two areas of the State that you assert are relevant economic retail electric power markets. Moreover, you suggest that the six percent market share is likely to decline by January 1, 2002, because the cooperatives do not have plans to increase their generating capacity in the interim, while other firms have announced plans either to increase existing plants or to enter the retail markets. You have also provided us information indicating that the joint marketing venture would have significantly lower retail distribution costs than would the individual cooperative members in serving state-wide or regional markets, and you have identified a significant

number of potential entrants into Arkansas retail distribution markets that can be expected to compete with the proposed joint venture.

On the basis of the information and assurances that you have provided to us, it does not appear that the proposal of the Distribution Cooperatives and AECC to form a joint retail marketing venture is likely to have any anticompetitive effects. The Distribution Cooperatives do not currently compete against each other in the generation of electric power, which they do jointly, or in the transportation of power, which they do within their own territories subject to regulation. Thus, the proposed joint retail marketing venture does not appear likely to have any adverse effects on either the electric power generation or transportation markets in Arkansas. While the Distribution Cooperatives could be viewed as potential entrants into each other's local retail markets, regional markets and a state-wide market, their relatively small size and lack of economies of scale and scope make it unlikely that they could enter new markets on their own or that, if they tried to enter, they would offer effective competition. In any event, the existence of other, larger potential entrants into those markets would significantly diminish, if not eliminate, any anticompetitive effect that might otherwise result from the joint venture proposal. It seems at least as likely, if not more so, that the joint retail marketing proposal would have the procompetitive effect of creating an additional entrant into retail markets not currently served by the Distribution Cooperatives.

For these reasons, the Department is not presently inclined to initiate antitrust enforcement action against the proposed joint marketing agreement. This letter, however, expresses the Department's current enforcement intention. In accordance with our normal practices, the Department reserves the right, in appropriate circumstances, to bring any enforcement action in the future if the actual operation of the proposed joint marketing agreement proves to be anticompetitive in any purpose or effect.

This statement is made in accordance with the Department's Business Review Procedure, 28 C.F.R. § 50.6. Pursuant to its terms, your business review request and this letter will be made publicly available immediately, and any supporting data will be made publicly available within 30 days of the date of this

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letter, unless you request that part of the material be withheld in accordance with Paragraph 10(c) of the Business Review Procedure.

Sincerely,

/S/

A. Douglas Melamed